

## Message Text

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ACTION EB-06

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PASS COMMERCE AND OPIC

E.O. 11652: N/A

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SUBJECT: FURTHER DETAILS ON BOUGAINVILLE COPPER NEGOTIATIONS

REF: A. PORT MORESBY 238; B. PORT MORESBY 263

1. SUMMARY: MAJOR PROVISIONS OF THE AGREEMENT SIGNED OCTOBER 16 BETWEEN THE GPNG AND BCL ARE ESSENTIALLY THOSE OUTLINED IN REFTEL B EXCEPT FOR THE PROVISION TO INVEST IN A SERIES OF MIDDLE-LEVEL PNG INDUSTRIES. ALTHOUGH APPARENTLY DISCUSSED, THE GOVERNMENT DECIDED THIS WOULD UNJUSTIFIABLY INCREASE BCL'S INFLUENCE AND THE PROVISION WAS NOT INCLUDED IN THE FINAL AGREEMENT. IN FINANCIAL TERMS, PNG WILL RECEIVE AN ADDITIONAL A\$55 MILLION IN REVENUE THIS YEAR WHICH AMOUNTS TO ABOUT 40 PERCENT TAXATION FOR THE FIRST HALF OF 1974. FUTURE TAX RUNS 33 1/3 PERCENT ON EARNINGS UP TO A\$87.2 MILLION AND 70 PERCENT ABOVE THAT FIGURE. THE INITIAL OUTCRY FROM SOME AUSTRALIAN NEWSPAPERS THAT THE RESULTS WERE "VIRTUAL EXPROPRIATION" HAS BEEN REPLACED WITH THE PROFESSED VIEW THAT THE AGREEMENT IS SOUND AND WILL ENCOURAGE CONTINUED INVESTMENT IN THE PNG MINERALS INDUSTRY. END SUMMARY.

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2. CHIEF MINISTER MICHAEL SOMARE ANNOUNCED THAT THE NEW AGREEMENT

WOULD GIVE PNG BETWEEN A\$200 AND A\$500 MILLION OVER THE NEXT TEN YEARS. THE NEW RATES WILL ENSURE A 15 PERCENT RETURN ON INVESTMENT AFTER TAXES, AND THE TAXES ARE LEVIED ON PROFITS, NOT REVENUES. THUS THE GOVERNMENT OBTAINED THE AGREEMENT IT SOUGHT WHEN SOMARE ANNOUNCED HIS DECISION TO RENEGOTIATE THE 1967 AGREEMENT LAST MARCH IN THE HOUSE OF ASSEMBLY. AT THAT TIME HE SAID THE PEOPLE OF PNG SHOULD RECEIVE A FAIR PRICE FOR THE MINERALS WHICH BELONGED TO THEM AND THAT FOREIGN MINING COMPANIES "ARE ENTITLED TO A FAIR RETURN ON THEIR INVESTMENT, BUT ONLY TO A FAIR RETURN. IF THERE ARE SPECTACULAR PROFITS CAUSED BY HIGH WORLD MARKET PRICES, PNG SHOULD RECEIVE THE LION'S SHARE OF THESE EXCESS PROFITS."

3. THE BCL IS NO LONGER ENTITLED TO ACCELERATED DEPRECIATION PROVISIONS WHICH COULD DELAY TAX PAYMENTS. NOR DOES IT ANY LONGER HAVE THE RIGHT TO EXCLUDE 20 PERCENT OF ITS INCOME. IT WILL ALSO NOT BE EXEMPT FROM NORMAL IMPORT DUTIES, STAMP DUTY, VEHICLE REGISTRATION FEES AND SIMILAR CHARGES. THUS ITS "STATE WITHIN A STATE" POSITION HAS BEEN EFFECTIVELY ELIMINATED.

4. NEW CONTROL AND NORMALIZATION PROVISIONS IN THE AGREEMENT SUBJECT BCL TO GENERAL LAWS ON: 1) ENVIRONMENTAL PROTECTION AND POLLUTION CONTROL; 2) IMPORTS AND EXPORTS; AND 3) APPROVAL OF CONTRACTS.

5. OF SPECIAL INTEREST TO THE PEOPLE OF BOUGAINVILLE ARE: A PROVISION FOR PAYMENT BY THE COMPANY OF 50 CENTS PER TON OF COPPER TO AN ENVIRONMENTAL FUND; A STUDY OF THE MINE'S IMPACT AND ANY NECESSARY CORRECTIVE MEASURES NEEDED; NO MORE PROSPECTING OR DEVELOPMENT OF ADDITIONAL MINES ON BOUGAINVILLE WITHOUT APPROVAL OF THE PEOPLE OF BOUGAINVILLE; AND THE ESTABLISHMENT OF A COMMITTEE BY THE BOUGAINVILLE PROVINCIAL GOVERNMENT TO DIRECT THE COMPANY'S BUSINESS ADVISORY SERVICE AND ELIMINATE ITS "RICH UNCLE" ABILITY TO INFLUENCE THE PEOPLE THROUGH SPECIAL GIFTS.

6. THE GPNG COMPROMISED ON TAXES WHEN IT ALLOWED THE BCL TO KEEP HALF OF THE EXCESS TAX THAT WOULD HAVE BEEN PAYABLE ON INCOME FROM THE FIRST SIX MONTHS OF 1974. THIS COST THE GOVERNMENT ABOUT A\$9 MILLION.

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7. ACCORDING TO "THE AUSTRALIAN FINANCIAL REVIEW", CONZINC RIOTINTO OF AUSTRALIA PUSHED UNSUCCESSFULLY FOR THE GPNG TO INCREASE ITS HOLDINGS FROM THE PRESENT 20 PERCENT, BUT THIS WAS REJECTED. INTERESTINGLY, THE COMPANY OFFERED SHARES AT 80 PERCENT ABOVE CURRENT MARKET PRICES INDICATING SHARE PRICES ARE SERIOUSLY UNDERVALUED. ONE MARKET ANALYST RECENTLY NOTED THAT AUSTRALIAN MINING SHARES WERE SELLING AT PRICE/EARNING MULTIPLES ALMOST DOUBLE THOSE FOR BCL. HAD THE GPNG ACCEPTED THE CRA OFFER TO

BUY AN ADDITIONAL 50 PERCENT OF THE SHARES, BRINGING ITS EQUITY TO 70 PERCENT, IT WOULD HAVE PAID A\$265 MILLION. AS NOTED IN REFTEL A, BOTH THE GOA AND THE GPNG REJECTED THE OFFER DESPITE VERY HEAVY PRESSURE FROM CRA. A LETTER FROM SIR VAL DUNCAN, CHAIRMAN OF RIOTINTO ZINC CORP., AND MR. ROD CARNEGIE, CHAIRMAN OF CONZINC RIOTINTO OF AUSTRALIA, TO MR. WHITLAM AND LEAKED TO THE PRESS STATED THAT THE PNG WAS DEMANDING 75 PERCENT OF THE CASHFLOW AND THIS "WOULD BE WIDELY RECOGNIZED AS THE EQUIVALENT TO EXPROPRIATION. WORLDWIDE PUBLICITY WOULD INEVITABLY FOLLOW, LEADING TO A SHARP DETERIORATION IN THE INVESTMENT CLIMATE PERCEIVED TO EXIST IN PNG. IT WOULD BE NATURAL IN THESE CIRCUMSTANCES FOR CRA TO APPEAL TO CANBERRA, AS ITS OWN GOVERNMENT, AND ESPECIALLY AS THE AUTHORITY WHICH ARRANGED AND APPROVED THE 1967 AGREEMENT." THE REQUEST WAS REJECTED OUT OF HAND AND NEGOTIATIONS WERE SHORTLY THEREAFTER SUCCESSFULLY CONCLUDED.

8. COMMENT: APPARENTLY THE GOA AND GPNG WERE KEEPING EACH OTHER FULLY INFORMED AS DEVELOPMENTS TOOK PLACE THUS REMOVING SOME OF THE PRESSURE DIRECTED TOWARD THE SOMARE GOVERNMENT. HIS GOVERNMENT HAS MADE CLEAR THAT IT IS VITALLY INTERESTED IN MAINTAINING A HEALTHY INVESTMENT CLIMATE AND THESE NEGOTIATIONS WERE A MOMENTOUS TEST CASE FROM WHICH THE GOVERNMENT EMERGED THE WINNER THUS SILENCING ITS MORE RADICAL, BUT LESS ASTUTE OPPONENTS AT LEAST FOR THE PRESENT.

9. ONE OF THE NEGOTIATORS TOLD ECON OFFICER THAT THE 15 PERCENT RETURN ON INVESTMENT WAS NOT A SET LEVEL, BUT THAT IN NEW INVESTMENT SUCH AS KENNECOTT'S OK TEDI VENTURE, THE PERCENTAGE WOULD BE HIGHER INITIALLY TO ATTRACT THE MAJOR CAPITAL NEEDED FOR DEVELOPMENT. THE PERCENTAGE ON RETURN WOULD BE SCALED DOWN AS THE VENTURE PROVED ITS PROFITABILITY. THUS THE GPNG IS TAKING A VERY PRAGMATIC ATTITUDE TOWARD ITS NEED FOR LARGE SCALE LIMITED OFFICIAL USE

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INVESTMENT AND THE NECESSARY RATE OF RETURN TO INVESTORS TO MAKE PNG ATTRACTIVE. END COMMENT.  
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## Message Attributes

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